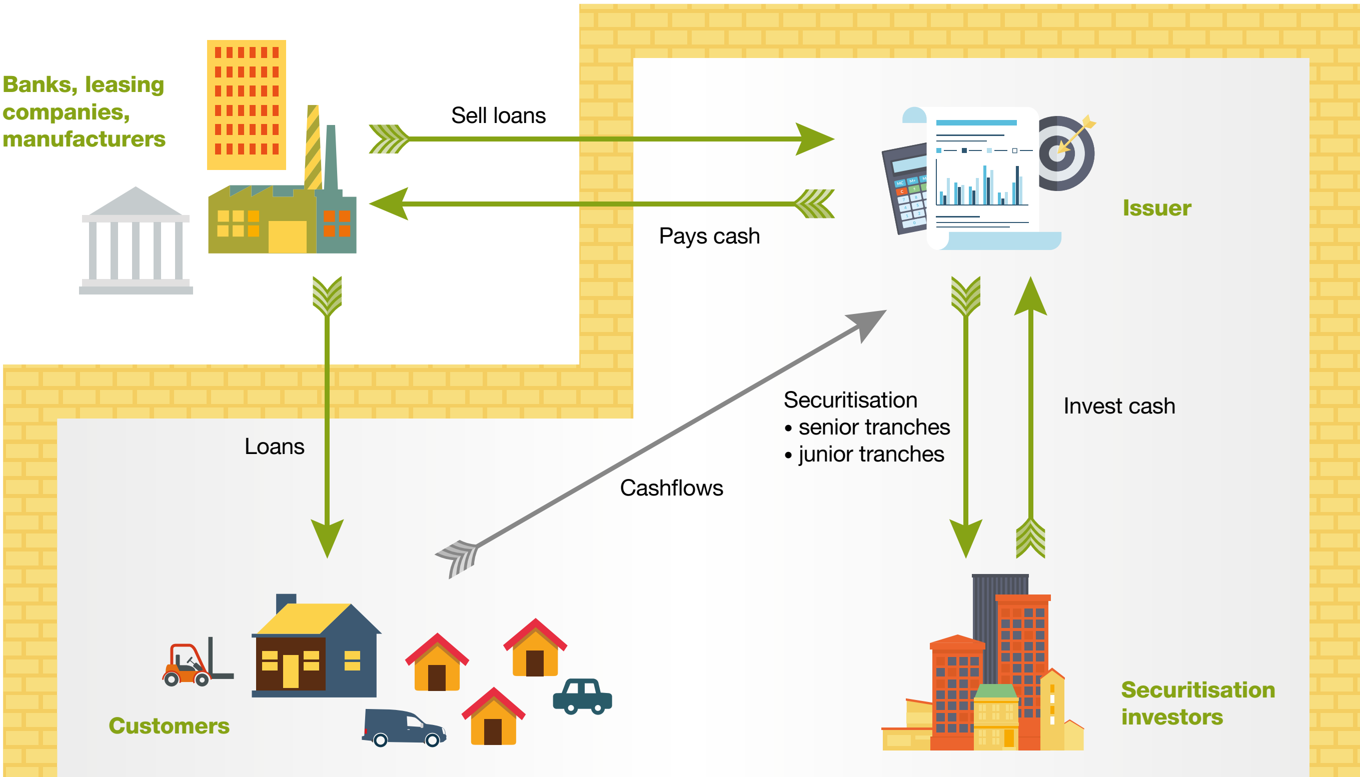
European securitisation: an essential tool to fund economic growth

What is securitisation?



Securitisation is a mechanism for financing real-economy assets by ring-fencing them and protecting the cashflows they generate for the benefit of institutional investors who receive what the ring-fenced assets generate. No more, no less.

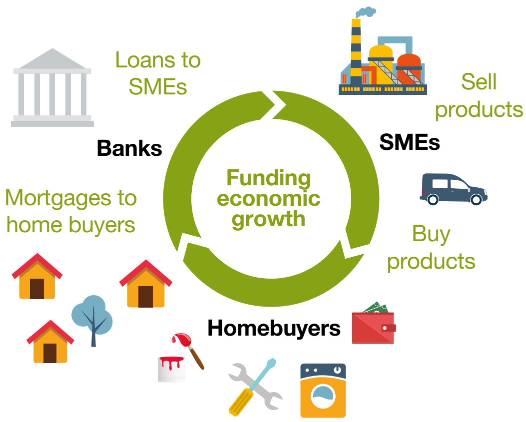
What are the benefits of securitisation for the real economy?

Securitisation can be a key source of financing at all stages of the supply chain

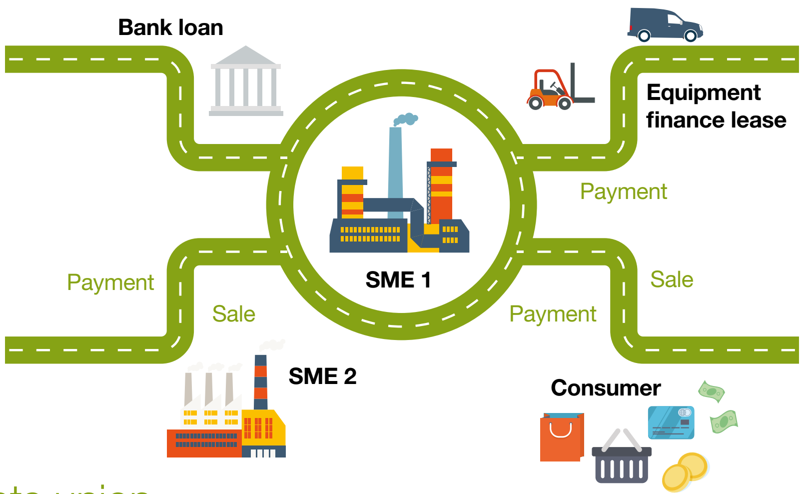
It can finance the cashflows of SMEs at many different stages in their business:

- **receivables owed by one SME to another**
- **helping the SME's customer to buy the ultimate product**

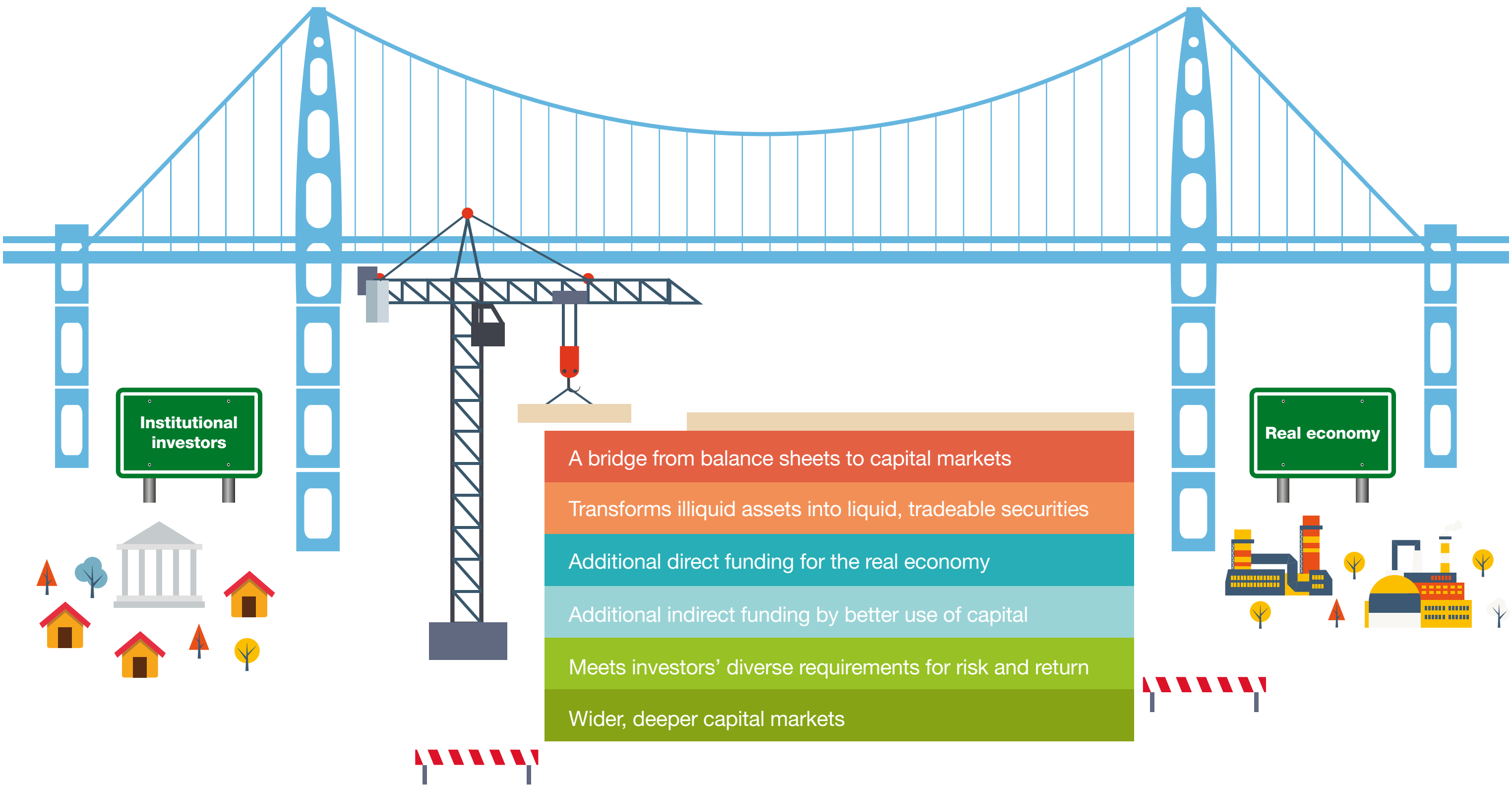
Securitisation can support SMEs in many ways



The benefits of securitisation are direct and indirect



Securitisation is key to capital markets union



How safe is securitisation?

EUROPEAN SECURITISATIONS

have performed extremely well

· THROUGH AND SINCE THE CRISIS ·

While no silver bullet, securitisation can undoubtedly help fuel economic growth thereby benefiting SMEs.

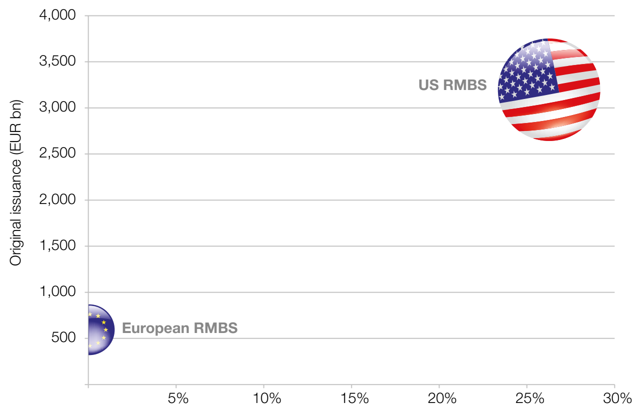
Securitisation also meets the needs of important institutional investors such as insurance companies and pension funds.

Although the European securitisation market has performed extremely well through and since the crisis, market volumes have decreased substantially over the years.

The numerous and very stringent STS criteria provide the necessary safeguards against the bad behaviour seen in the US sub-prime mortgage market.

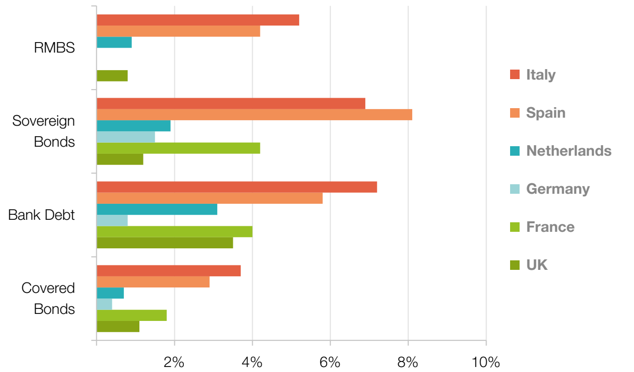
The proposed framework for simple, transparent and standardised securitisation and accompanying recalibration rules have the potential to revive the European securitisation market for the benefit of the overall economy.

Unlike in the US, European default rates have been very low...



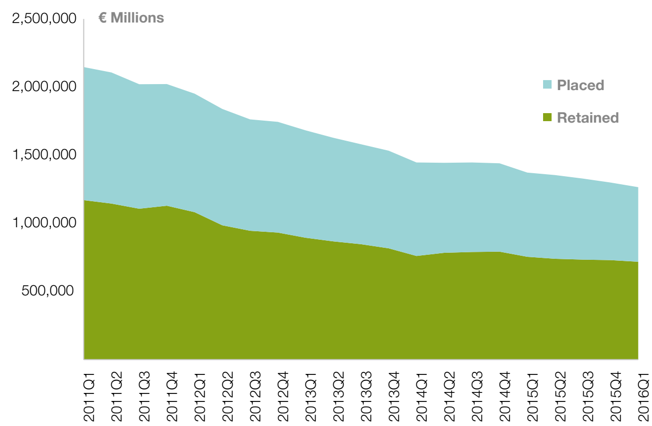
Historical default rates for residential mortgage-backed securities (RMBS), 2007–2015. Source: S&P Global Ratings.

and European RMBS market price performance compares well with sovereigns, bank debt and covered bonds...



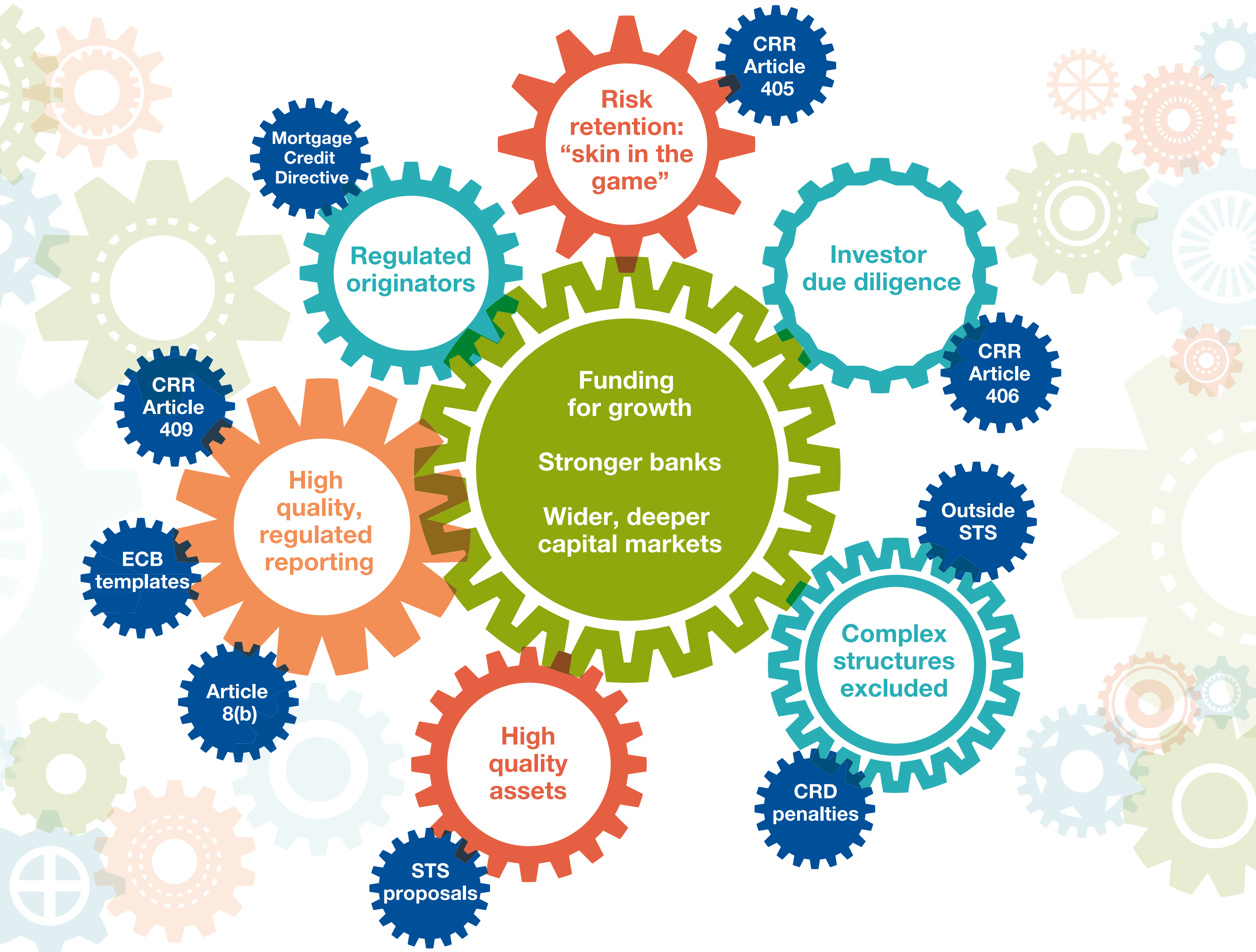
Credit spread volatility by asset class, January 2011–March 2012. Source: Bank of America Merrill Lynch.

yet the market continues to shrink...



European securitisations outstanding.
Sources: AFME/SIFMA members, Bloomberg, Dealogic, Thomson Reuters, AFME & SIFMA.

European securitisation is already strongly regulated. The STS proposals add yet more protection.



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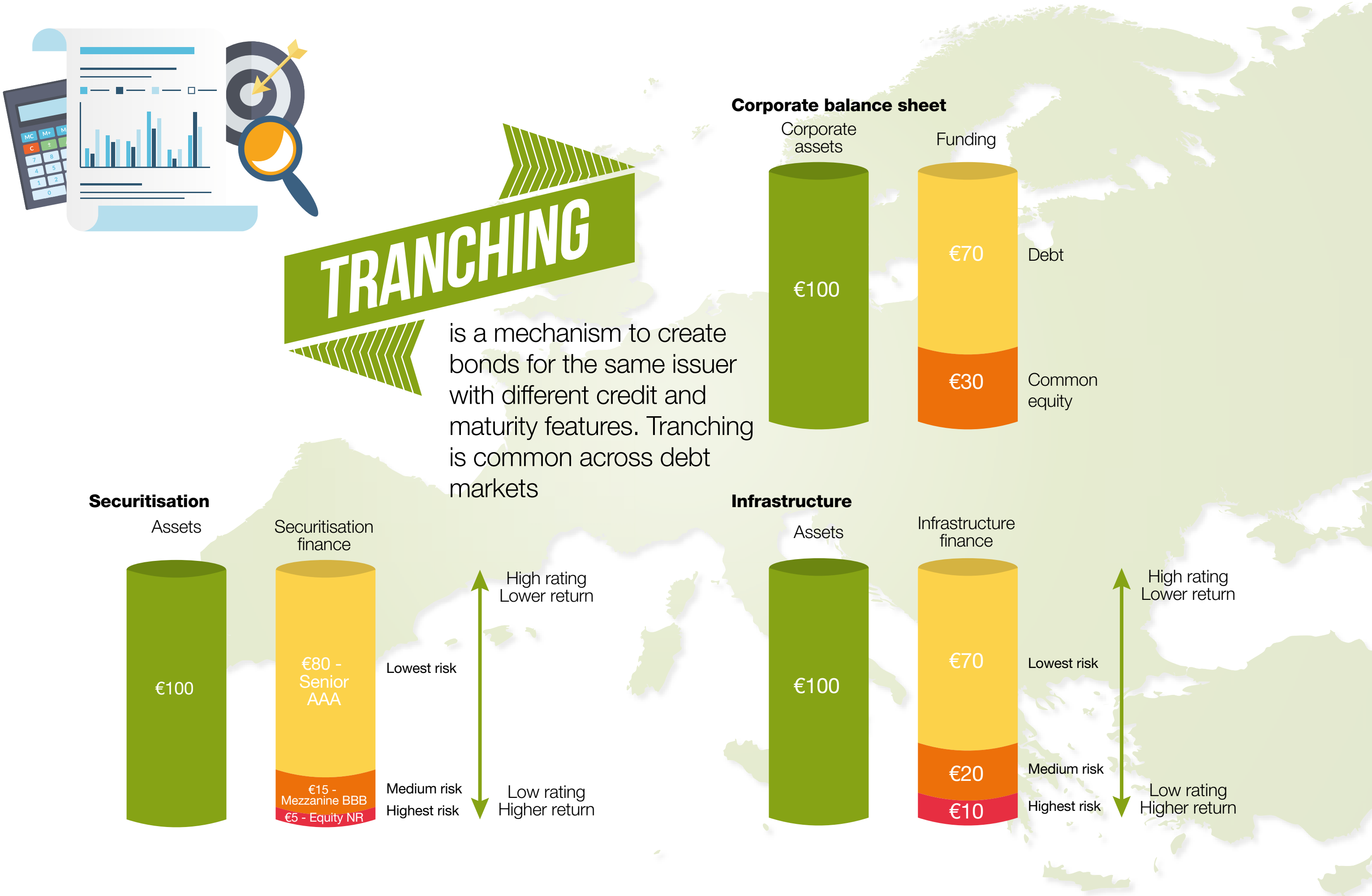
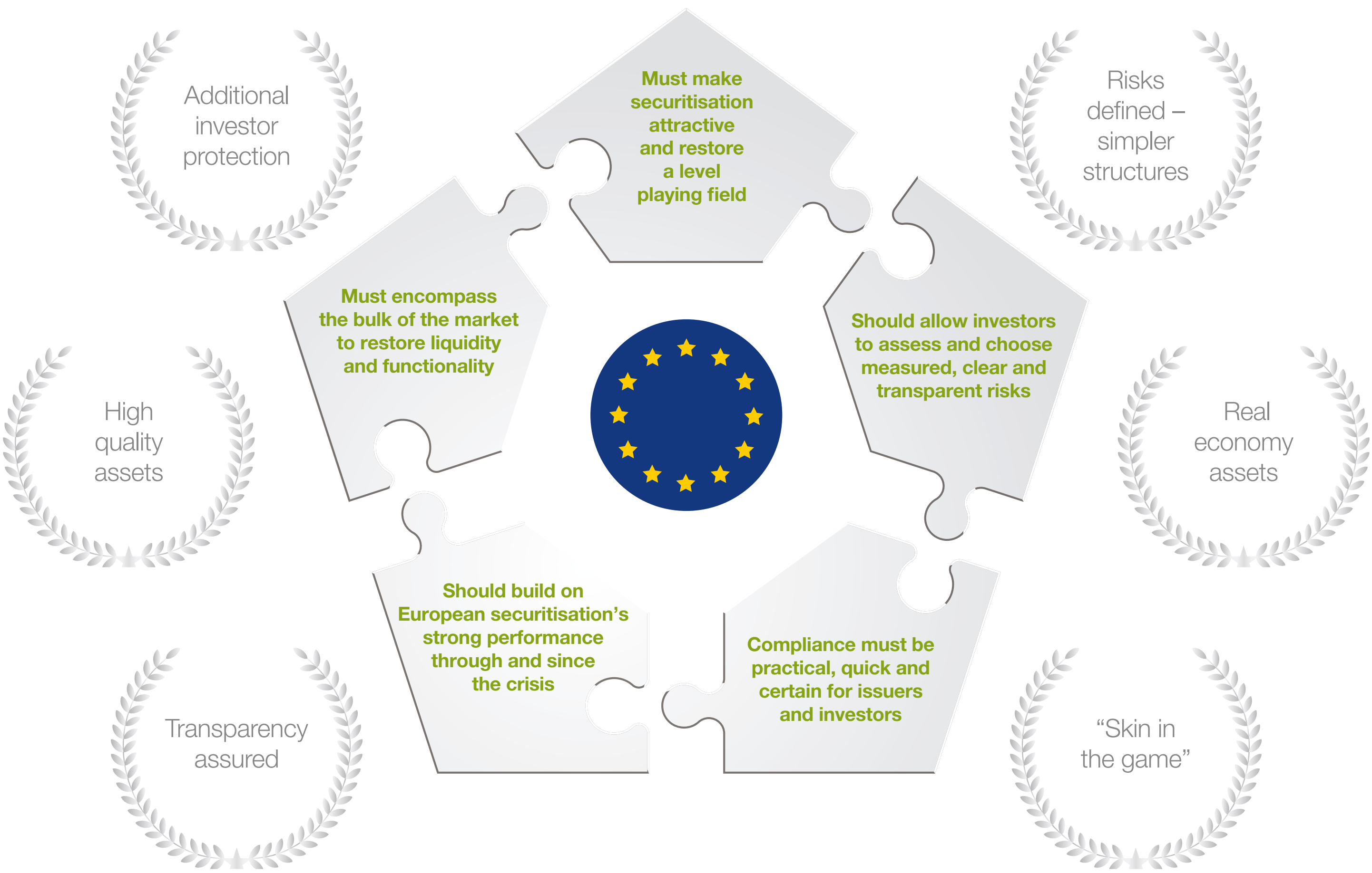
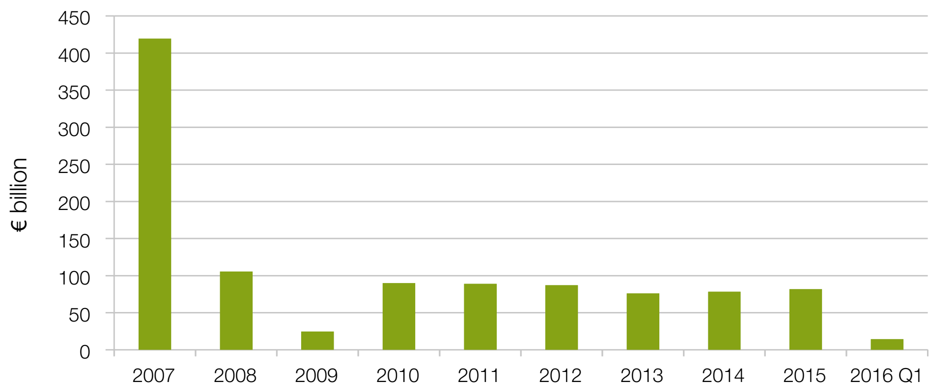


Key principles for, and benefits of, STS



Reviving securitisation, promoting growth

"Securitisation markets are a key funding channel for the economy, increasing the availability and reducing the cost of funding for households and companies by opening up investment opportunities to a wider investor base, diversifying risk across the economy and freeing up bank balance sheets to lend." Commissioner Jonathan Hill at the Eurofi Financial Forum, September 2015



European ABS issuance (Sources: Bloomberg, Citigroup, Dealogic, Deutsche Bank, JP Morgan, Bank of America-Merrill Lynch, RBS, Thomson Reuters, UniCredit, AFME & SIFMA)

EU securitisation markets have been shrinking significantly in recent years. A reversal of this trend will require a forward-looking approach by policy makers.

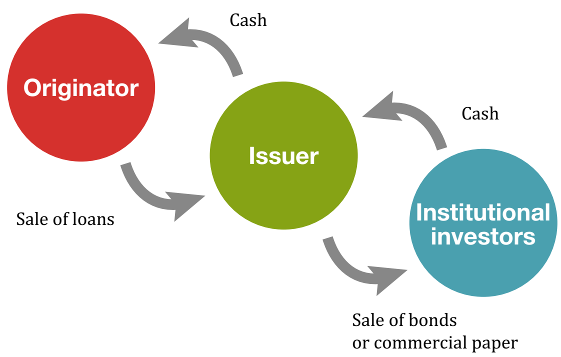
Is securitisation safe?

For some, securitisation still suffers from the stigma associated with its misuse before the crisis. However, it is vital to recognise that, while some securitisations – for example, subprime mortgages in the US – performed badly, European securitisations have performed well, through and since the crisis. Securitisation is nothing more than a financing technique and, when used sensibly, can help banks raise funding, and support new lending to SMEs and other key players in the real economy.

A broad range of regulations and industry initiatives has been put in place since the crisis, ensuring better alignment of risk between issuers and investors. In addition, greater transparency requirements enable investors better to assess risks. Reliance on credit ratings has been reduced, and rating criteria tightened. This will provide the basis for a new, sustainable market for simple, transparent and standardised securitisation in Europe.

What is securitisation?

Securitisation is the process of pooling together a large number of loans (such as mortgages, auto loans or SME loans) held on the balance sheet of a bank or other financial institution (the Originator) and selling them to a newly created and legally separate entity (the Issuer). This entity finances the purchase of the loans by issuing bonds to investors. The loans generate cashflows (for example, monthly mortgage payments from homeowners), which are used to repay the investors. In this way, loans which would otherwise be illiquid can be converted into more liquid and tradeable securities.



Because large numbers of loans are used, statistical analysis can determine the likelihood that some of them will default. Therefore, the bonds can be divided into different tranches with varying levels of risk. The lower-risk tranches can raise funding on very attractive terms while higher-risk tranches yield a higher return for investors.

Why is it important?

At a time when bank lending is constrained, securitisation can boost both credit and growth. For example, a carmaker, expecting lots of monthly payments from customers who have taken out financing, can get investors to fund its business more cheaply by selling them its claim to those payments. A bank receiving mortgage repayments can bundle such loans up and sell them or use them as collateral to get funding, which it can then use to issue more loans to the real economy. Securitisation can be a vital funding tool in Europe and a channel for borrowers to access the capital markets.